NOTES

CONVERSION OF WAR-RISK POLICIES

Interest in the federal government's experiment in war-risk insurance centers in the propaganda to prevent lapses and hasten the process of conversion of term policies into the permanent forms of insurance, details of which were published last spring. At an investigation conducted by the War Risk Bureau's Advisory Commission in July, it was reported that over 3,000,000 of the 4,000,000 policyholders have ceased the payment of premiums. These are not necessarily lost, however, as under the present ruling of the Secretary of the Treasury discharged soldiers, sailors, and marines who have dropped or canceled their policies may reinstate within eighteen months after their discharge without payment of back premiums, except for the month of grace when under the regulations the policy continued in force. The only limitation on the privilege is that the applicant shall be in as good health as he was at the date of his discharge. Urgent appeals are being made to secure reinstatements and to prevent a continuance of the enormous lapse rate.

A very large proportion of the holders of these policies are young men without dependents who for several years in the normal course of events would not have been in the market for insurance, or would at most have taken a two- or three-thousand-dollar policy. To these as well as to others who were provided before entering the service with what they considered adequate insurance, the decision whether to lapse or convert their policies presents in many cases a difficult problem. A comparison between the converted policies and those offered by private companies is therefore of some interest.

In the first place, it may safely be assumed that the choice between government insurance and private insurance is one in which the holder of the war-risk policy may properly be governed by personal motives. It has occasionally been urged that there is a patriotic obligation on the healthy policyholders to keep up their policies in order that the Bureau may be shielded from adverse selection, which it must be admitted is a serious menace to the scheme in view of the large number of disabled veterans among the insured. The obligation to furnish insurance without extra cost to these "poor risks," however, is an obligation of

the nation in whose service they became poor risks, not of their more fortunate comrades who may have the opportunity of securing insurance in companies not so heavily burdened with the wreckage of war. It is difficult to see, however, how the existence of a mass of policies covering substandard lives presents a real objection to the government's insurance plan from the standpoint of the healthy policyholder. In a private company an accumulation of poor hazards might raise a question as to the adequacy of reserves and the ultimate security of the policy, but with the taxing power of the United States pledged to the payment of every legitimate claim the question of adequacy of reserve is irrelevant, from the policyholders' standpoint.

Next in importance to the question of safety stands that of the terms of the contract. The War Risk Bureau offers the option of conversion into "whole life" policies, twenty- or thirty-year limited payment or endowment policies, or endowment policies maturing at age 62. Most of the liberal policy features developed by legislation or by the keen competition of life insurance companies in recent years are included—high loan and surrender values, option of monthly, quarterly, or annual premium payments, exemption of proceeds from taxation and from the claims of creditors, and incontestability from date of issuance, the last provision one which seems to offer an unnecessary incentive to fraud. The disability clause is extremely liberal, providing for payment of $5.75 per thousand dollars insurance monthly for the period of total disability, or for 240 months in case of death before the expiration of that period. Similar clauses in private insurance contracts usually cover only disability incurred before a specified age, 60, 65, or 70 years. In view of the very large proportion of aged persons who incur disability, this feature is of considerable importance.

The only respects in which the Bureau's policy appears less liberal than the usual commercial policy are, first, the rather narrow list of eligible beneficiaries, a matter of little practical importance, and second, the provision for payment of all claims (except matured endowments) in 240 monthly instalments, with interest at $3\frac{1}{2}$ per cent, or in an annuity on the life of the beneficiary. In a very large number of cases the instalment or annuity settlement is much better than cash, from the standpoint of the beneficiary's real interest, and the Bureau has performed an excellent service in calling forcible attention to the advantages of these forms of settlement, which have been used comparatively little in this country. Nevertheless it is urged with some force that if the insured prefers to provide for a cash settlement he should be allowed

to do so, and legislation to remove this limitation is now under consideration.

It is unfortunate that term insurance has been excluded from the list of permanent policies. Term insurance contracts expiring at the close of the insured's earning capacity, or shorter term policies renewable without examination, afford the maximum of pure protection at the minimum cost, and might better be carried by many policyholders who are accepting smaller protection than they need for the sake of a moderately desirable investment contract. Term policies are not popular, the candidate for insurance being apt to infer that if he lives out the term of the contract he has given something for nothing. The hostility of most insurance companies to term insurance has encouraged this attitude. The War Risk Bureau had an opportunity to do an excellent piece of educational work on this point, but has chosen instead to adopt the traditional viewpoint, treating the term policy as a makeshift and urging early conversion into the more "permanent" types of investment policy.

The real comparison, however, must be on the basis of cost. The rates charged on all the government policies are net, figured on the American Experience mortality table and a $3\frac{1}{2}$ per cent interest basis. Comparison with rates charged by private companies is difficult, as the government policies are of the participating type, and the net cost depends on the size of the dividends, which in turn depends on the mortality rate and the interest earnings, expenses being paid by the government. No information is available concerning the manner in which earnings are being obtained or computed, but the very high mortality rate during the war, the large number of poor risks, and the high lapse rate with its accompanying adverse selection make it probable that the prospect of dividends is a negligible factor. The more important the liberal disability clause proves to be in practice the more remote of course becomes the prospect of dividends. Comparison of government rates with commercial rates for non-participating policies is therefore not unfair.

The lowest rates charged for standard policies are only a trifle higher than the government net rates, the bulk of the expenses being paid by insurance companies out of mortality savings and interest gains.[1]

[1] The lowest specimen rates quoted in the 1918 report of the Connecticut Insurance Commissioner are from thirteen cents to two dollars per thousand higher than the government rates. Some companies charge considerably more. These rates, however, do not cover disability insurance. Computations of the value of the clause in the Bureau's form are not available, but much less liberal clauses are rated as worth an addition of as much as 8 per cent to a whole life premium.

The incentive, therefore, for a policyholder in good health to keep up his premium payments rather than lapse with a view to securing insurance elsewhere when it is needed may be summarized as follows: the value of the disability clause, plus the small saving in direct premium charge, plus the remote prospect of dividends, minus the saving in cost of insurance from the time of lapse to the time when the insurance will be needed. Certainly the Bureau's policies are on the bargain counter, and the question arises, Why the tremendous difficulty in convincing the policyholders of their merit?

The chief explanation, aside from the incorrigible disposition of the human race to postpone the purchase of life insurance till it cannot be secured, is probably to be found in dissatisfaction with the administration of the War Risk Bureau. Certainly the delays and clerical and administrative errors in the Bureau would have wrecked the business of any private company. This is not strange, considering the difficulties of organizing such a vast enterprise under the conditions which surround administration in Washington. No one familiar with these conditions will be surprised if much more time is required before the War Risk Bureau attains the efficiency of a well-conducted private insurance company, but neither will such a one allow his judgment of the value of the Bureau's offerings to be warped by irritation at its clerical shortcomings. Though our bureaucratic machinery grinds slowly it usually grinds small enough at last to satisfy the most fastidious.

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